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Ecuadoran President Mahuad's Administration Facing Multiple Crises

by LADB Staff

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In September, Ecuador declared a moratorium on its discount Brady bonds (see NotiSur, 1999-10-01) and in late October extended its restructuring plan to all debt except agreements with multilateral lending institutions.

Meanwhile, Congress has still not passed legislation needed to finalize an agreement with the International Monetary Fund (IMF), and President Jamil Mahuad has become embroiled in a debilitating financial scandal. Ecuador is struggling with a crushing foreign debt, currency devaluation, and the highest inflation in Latin America.

And President Mahuad's government has also faced a year of political infighting and often violent demonstrations by students, transportation workers, and Indian groups (see NotiSur, 1999-07-16). Unemployment rose from 13% in August 1998 to 18.1% with 54.4% underemployment in September 1999. Economic growth is expected to contract by up to 7% this year, and annual inflation is projected at 50%.

The nation's total public debt of US\$13 billion will likely top 117% of GDP by the end of the year. A US\$400 million loan agreement with the IMF, expected to bring another US\$1 billion in international aid, hinges on Congress approving reform legislation and a balanced budget for 2000. New protests threaten the administration as it tries to break the congressional impasse.

The Coordinadora de Movimientos Sociales (CMS), which includes unions and indigenous, and social organizations, has threatened to call a "popular uprising" if the executive does not fulfill commitments made months ago. On Oct. 25, Ecuador's military took the unusual step of publicly criticizing the "irresponsible conduct" by "certain leaders" that is threatening democracy. "It's absurd and dangerous that certain leaders and political, economic, and social groups use their power to provoke constant clashes, scandals, and strikes without offering any significant strategies or objectives beyond electoral and material ones," the statement said. The military demanded that the problems be immediately resolved and called for the support of all Ecuadorans.

On Oct. 30, Defense Minister retired Gen. Jose Gallardo said many Ecuadorans have approached the armed forces to intervene in the political crisis in the country. Mahuad extends debt default On Oct. 22, Ecuador said it would defer US\$27.3 million in payments due on its US\$500 million in Eurobonds and would defer another US\$33.1 million payment on PAR Brady-bond interest due in November.

The government said its restructuring plan would also include 50% of the total internal debt of about US\$2 billion. "The nation has decided to confront its public debt issue with a global strategy," Finance Minister Alfredo Arizaga told reporters. "It's in the process of renegotiating its Brady bonds, Eurobonds, Paris Club, and internal debt."

Analysts had mixed reactions to Ecuador's decision. Some applauded the action saying a global, total assault on the nation's debt was necessary to cure the problems. Others said it would further complicate talks with creditors and choke access to loans. "This is the only half-decent idea they've come up with after a series of bad steps by the [debt] negotiating committee," said economic analyst Jorge Ambram. But Ernesto Pinto, an analyst with economic research firm Pacificdata, said the move threatens to destroy whatever tattered image Ecuador had left with investors.

On Oct. 26, Ecuador began negotiations in New York with hedge funds, mutual funds, and other investors who hold the country's bonds. "We are going to listen to what they have to say," said Marc Helie, managing director at Gramercy Advisors, which is representing bondholders that have come together under the name of Ecuador Creditors Advisory Group Inc.

UNICEF calls for debt relief

Meanwhile, the United Nations Children's Fund (UNICEF) warned that, if the Ecuadoran situation does not change significantly, half the population would likely be living in poverty next year. The UNICEF office in Quito has said that the percentage of Ecuadorans surviving on less than US\$2 a day has risen from 38% to 44% in the past 12 months. "While it is unusual for UNICEF to focus on the complexities of debt reduction in an individual country, the situation in Ecuador is so severe and so fraught with risk for children and women that we must speak out," UNICEF Executive Director Carol Bellamy said.

Bellamy said one cause of the crisis, which threatens a dramatic deterioration in the health and well-being of the population, particularly the children of poor families, is the debt burden. It severely limits the resources available for social programs. For example, in 2000, debt servicing will take more than half the proposed government budget.

Meanwhile, social spending has been reduced by US\$76 million, including a US\$37 million reduction in education programs. "While Ecuador's debt obligations were undoubtedly incurred in good faith, the servicing of the debt must not be at the cost of the health and well-being of its citizens, particularly the children," she said. "If Ecuador's external debts can be renegotiated in such a way as to lessen the crushing burden of debt repayment, and hence allow the government to dedicate greater resources to social programs, this would set an important precedent for other Latin American countries."

Congress still bickering about reforms

Mahuad's budget proposal has been stalled for weeks in Congress as rightist parties oppose tax increases and left-of-center opponents object to spending cuts, especially for social programs. On Oct. 26, Congress finally approved a number of crucial reform measures including increases in value-added taxes (impuesto al valor agregado, IVA), income taxes, and corporate taxes. Another vote is needed, however, to finalize the reforms. The estimated US\$450 million in additional income these tax changes would bring would allow the government to reach its goal of running a budget deficit of between 2% and 2.5% of GDP.

Both fiscal reform and budgetary approval are conditions in the IMF letter of intent. The measures, which raise the IVA from 10% to 12% and increase the corporation tax and the maximum level of

income tax to 25%, were approved by 51 of the 97 deputies who voted. Mahuad accused of campaign irregularities On Oct. 21, jailed banker Fernando Aspiazu filed a motion with the Corte Suprema de Justicia (CSJ) accusing Mahuad's former chief of staff Ramon Yulee of irregularities in the use of campaign monies during Mahuad's presidential campaign. Yulee was treasurer of the campaign.

Aspiazu, former president of the Banco del Progreso, was accused of mismanagement of funds after the bank went under last April. In July, the government ordered his arrest on charges that he withheld some of the tax on banking transactions charged to bank clients an irregularity reported months earlier without any action being taken. Aspiazu's lawyer, Jorge Zavala, said that during the campaign the banker gave US\$3.1 million to Mahuad's campaign, which was never declared.

Ecuadoran law requires that, after the elections, presidential candidates file a list of their campaign contributions with the Tribunal Supremo Electoral (TSE). Aspiazu said his contribution was not on the declaration presented by governing Democracia Popular (DP). Mahuad will be called to testify before the court investigating the alleged misuse of campaign contributions, said Guayaquil criminal court Judge Isabel Segarra on Oct. 25. On Nov. 3, Mahuad dismissed the charges, but said next week he will make available a full accounting of campaign contributions.

The president accused Aspiazu of bringing the Banco del Progreso to bankruptcy and jeopardizing the deposits of 700,000 clients. He said the banker's accusations were a smokescreen to cover his own crimes. The process has brought an intense legal and constitutional debate.

Former CSJ president Carlos Solorzano said under the Constitution the president can only be tried when Congress authorizes it and then through a process established by the legislature. "This suit has been politically manipulated," said Solorzano, adding that Aspiazu has the backing of the opposition Partido Social Cristiano (PC).

The latest scandal erupted just as Transparency International released its annual Corruption Perceptions Index, ranking Ecuador among the three most graft-ridden countries in Latin America, after Honduras and Paraguay. [Sources: Associated Press, 10/25/99; The Financial Times (London), 10/27/99; Inter Press Service, 10/28/99; Clarin (Argentina), 10/29/99; Reuters, 10/22/99, 10/26/99, 11/01/99; Excelsior (Mexico), 11/02/99; Notimex, 10/23/99, 10/31/99, 11/03/99; Spanish news service EFE, 10/21/99, 10/23/99, 10/26/99, 10/29/99, 11/04/99]

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